

Message Text

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SUBJ: SWISS ECONOMY: REVIEW OF 1976 AND OUTLOOK FOR 1977

1. SUMMARY: SWISS ECONOMY HAS BEEN UNABLE TO GENERATE
SUSTAINED RECOVERY FROM THE RECESSION. MOST EXPORT
INDUSTRIES (KEY TO RECOVERY) ARE STILL EXPERIENCING
REDUCED FOREIGN DEMAND TO WHICH SWISS FRANC APPRECIATION
AND STRUCTURAL WEAKNESSES WITHIN SOME KEY INDUSTRIES
(PARTICULARLY WATCHES) HAS CONTRIBUTED. ECONOMY
STABILIZED SOMEWHAT IN 1976 WITH ONLY SLKGHT REAL
DECLINE IN GNP AFTER 7.7 PERCENT DROP IN 1975. ALMOST
NO REAL GROWTH FORECASTED FOR 1977 THOUGH NOMINAL GNP MAY
RISE 2 PERCENT. UNUSUAL, FOR SWITZERLAND, TRADE SURPLUS
IS RESULT OF LOW DOMESTIC DEMAND. SWISS NATIONAL
BANK BELIEVES UPWARD PRESSURE ON SWISS FRANC WILL
CONTINUE IN 1977 BUT LESS ACUTELY WITH US DOLLAR APPRE-
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CIATING AGAINST SWISS FRANC. MOST ECONOMISTS OPTIMISTIC
FOR LONGER TERM BECAUSE OF PRESENT LOW RATE OF UN-
EMPLOYMENT AND INFLATION, LOW INTEREST RATES AND HIGHLY
LIQUID CAPITAL MARKET. FORECAST OF POSSIBLE INCREASED
UNEMPLOYMENT THIS YEAR HAS PROMPTED CALLS FOR
GOVT INITIATIVES TO STIMULATE THE CONOMY. END SUMMARY.

2. SWISS ECONOMY RECOVERY DEPENDS ON STIMULUS GENERATED BY INCREASED DEMAND FOR SWISS EXPORTS. HOWEVER, EXPECTATIONS OF EARLY SWISS RECOVERY FADED WHEN SWITZERLANDS MAJOR TRADING PARTNERS (EC AND US) ENTERED PERIOD OF "ECONOMIC PAUSE" AT MID-YEAR. CONSEQUENTLY, SHORT-TERM PROSPECTS ARE NOT GOOD FOR INCREASED SALES AT PRICE LEVEL WHICH WOULD IMPROVE CURRENTLY UNSATISFACTORY CASH-FLOW POSITION OF KEY INDUSTRIES WHICH NORMALLY EXPORT ABOUT 80 PERCENT OF PRODUCTION. OVERALL, INDEX OF INDUSTRIAL PRODUCTION MAY HAVE RISEN SLIGHTLY IN 1976. BUT PLANT CAPACITY REMAINED ABOUT 78 PERCENT UTILIZED. SEVERAL OF LARGEST SWISS CORPS WERE ABLE TO INCREASE 1976 OUTPUT AND RECEIPTS, BUT MOST HAD REDUCED EARNINGS DUE TO PRICE REDUCTIONS MADE IN ORDER TO MAINTAIN MARKET POSITIONS ABROAD.

3. DOMESTIC CONSUMPTION SHOWED LITTLE IF ANY REAL INCREASE LAST YEAR, LARGELY AS RESULT LOSS OF 300,000 JOB POSITIONS IN PAST TWO YEARS WHICH WAS ABSORBED BY DEPARTURE 200,000 FOREIGN WORKERS AND MANY SWISS FROM LABOR FORCE. UNEMPLOYMENT RATE FELL TO 0.5 PERCENT END 1976 FROM 1.1 PERCENT END 1975. BUSINESS FAILURES ROSE 7.7 PERCENT LAST YEAR. FURTHER RATIONALIZATIONS, PARTICULARLY IN WATCH INDUSTRY, COULD RESULT IN LOSS ADDITIONAL 30,000 JOB POSITIONS IN 1977. THOUGH BUSINESSMEN GENERALLY OPTIMISTIC ABOUT EARLY 1977 SALE SOUTLOOK, THEY FIND IT INCREASINGLY DIFFICULT TO JUDGE MARKET TREND.

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4. FOREIGN TRADE IN 1976 AVERAGED 12 PERCENT GROWTH IN REAL TERMS, AND A 6 PERCENT INCREASE IS EXPECTED IN 1977. HOWEVER, VALUE OF IMPORTS REMAINED BELOW THAT RECORDED IN 1974. CAPITAL GOOD IMPORTS DECLINED AND APPRECIATED SWISS FRANC (UP 10.4 PERCENT ON TRADE WEIGHTED BASIS IN 1976) HELPED REDUCED IMPORT COSTS. THESE FACTORS PRODUCED 1976 TRADE SURPLUS ABOUT \$1.3 BILLION, FIRST SURPLUS SINCE 1953 AND ONLY FOURTH THIS CENTURY. ESTIMATED 1976 CURRENT ACCOUNT SURPLUS ABOUT \$3.4 BILLION; 1977 CURRENT ACCOUNT SURPLUS OF \$3.6 BILLION EXPECTED BUT FORECAST IS FOR A TRADE DEFICIT. OIL PRICE INCREASE EXPECTED TO HAVE LITTLE IF ANY SHORT-TERM IMPACT ON SWISS ECONOMY.

5. GOVT AND SWISS NATIONAL BANK POLICIES AIM AT CREATING CONDITIONS FOR SPEECY RECOVERY ONCE PACE OF GROWTH PICKS UP IN MAJOR SWISS EXPORT MARKETS. CONSUMER PRICE INDEX ROSE 1.2 PERCENT IN 1976 (COM-

PARED 6.7 PERCENT 1975) DUE TO LOWER IMPORT PRICES, APPRECIATED SWISS FRANC AND GOVT POLICY TO HOLD DOWN PRICES AND COSTS. SIMILAR INFLATION RATE EXPECTED IN 1977 WITH ONLY SLIGHT REAL WAGE INCREASE IN BOTH YEARS TO KEEP PACE WITH PRICES. NATIONAL BANK HAS SOUGHT TO CURB RAPIDLY APPRECIATING FRANC EXCHANGE RATE BY TIGHTENING MEASURES AIMED AT DISCOURAGING FOREIGN DEMAND FOR SWISS FRANC AND ENCOURAGING CAPITAL EXPORTS. NATIONAL BANK 1976 INTERVENTIONS ON FOREIGN EXCHANGE MARKET TO STABILIZE EXCHANGE RATE FLUCTUATIONS PRODUCED NET \$1.3 BILLION INCREASE IN FOREIGN EXCHANGE HOLDINGS. THOUGH FRANC EXPECTED APPRECIATE 5 PERCENT IN 1977, SWISS AUTHORITIES EXPECT IT TO CONTINUE TO DEPRECIATE AGAINST US DOLLAR THIS YEAR AS US ECONOMY IMPROVES

6. INCREASED CAPITAL MARKET LIQUIDITY CAUSED SHORT TERM INTEREST UNCLASSIFIED

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RATES TO DROP AVERAGE 50 PERCENT AND LONG TERM RATES 25 PERCENT IN 1976. INTEREST RATES EXPECTED TO DECLINE FURTHER IN FIRST QUARTER 1977, THOUGH PUBLIC SECTOR BORROWING AT UNPRECEDENTED RATE AND INCREASED LEVEL OF FOREIGN BOND ISSUES ON SWISS CAPITAL MARKET HAVE SOAKED UP SOME LIQUIDITY. SWISS MONEY SUPPLY (M1) EXPANDED BY OVER 6 PERCENT IN 1976, 5 PERCENT GOAL IN 1977. LIBERAL MONETARY POLICY IS AIMED AT HELPING FINANCE INVESTMENTS NECESSARY FOR RECOVERY WITHOUT FUELING INFLATION. HOWEVER, ECONOMISTS ARGUE THAT LOW INTEREST RATES ALONE WILL NOT STIMULATE SUFFICIENT INVESTMENT IN PRESENT UNCERTAIN CLIMATE. INVESTMENTS IN NEW PLANT AND EQUIPMENT FELL ESTIMATED 8.5 PERCENT IN 1976, 4.5 PERCENT INCREASE IS FORECAST FOR 1977.

8. THERE ARE INCREASING CALLS FOR GOVT INITIATIVES TO STIMULATE DEMAND, THOUGH PRESENT STATE OF PUBLIC FINANCES PROVIDE LITTLE ROOM FOR SUCH MEASURES. GOVT OFFICIALS HAVE MENTIONED POSSIBLE \$800 MILLION SPENDING PROGRAM IN LATE 1977 IF UNEMPLOYMENT BECOMES SERIOUS. HOWEVER, NATIONAL BANK VICE PRESIDENT RECENTLY WARNED THAT PUBLIC AUTHORITIES DEFICIT SPENDING AND HIGH BANK LIQUIDITY CARRY LONG TERM DANGER OF RE-NEWED INFLATION PRODUCING INCREASED UNEMPLOYMENT. PRESS HAS CALLED 1977 YEAR OF CRUCIAL DECISIONS FOR SWISS WHO WILL VOTE ON PROVIDING GOVT BROADER ECONOMIC POLICY POWERS AND VALUE ADDED TAX TO BOOST GOVT REVENUES.

9. AGRICULTURAL OUTPUT IS FORECASTED TO RISE 3.7 PERCENT IN 1977 TO ABOUT \$2.8 BILLION, 5 PERCENT OF GNP, COM-

PARED TO 4.6 PERCENT IN 1976. SWISS AGRICULTURAL
POLICIES ARE EXPECTED TO CONTINUE TO IMPOSE MORE
RESTRICTIVE IMPORT MEASURES IN SUPPORT OF GREATER
DOMESTIC PRODUCTIVITY AND SIMULTANEOUSLY SEEK TO
EXPANDED OUTLETS FOR PROCESSED PRODUCTS, ESPECIALLY
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IN THE SURPLUS PRONE DAIRY SECTOR WHERE EXCESSIVE
AMOUNTS OF FRESH MIL SEEK FOREIGN MARKET ACCESS IN
THE FORM OF PRODUCTS. TO REACH TO 1980 OBJECTIVE OF
EXPANDED BREAD AND FEED GRAIN ACREAGE, HIGHER DOMESTIC
GUARANTEES SUPPORT PRICES WILL PROBABLY BE NECESSARY,
WHICH MUST THEN BE PROTECTED FROM COMPETITIVE IMPORTS
BY HIGHER LEVIES AND/OR RESTRICTIVE QUOTAS.
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